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Nos. 94-1977, 94-1995

IN THE
Supreme Court of the United States

OCTOBER TERM, 1994

JERSEY CENTRAL POWER & LIGHT COMPANY,

Petitioner,

v.

FREEHOLD COGENERATION ASSOCIATES, L.P.,

Respondent.

THE NEW JERSEY DIVISION OF THE RATEPAYER ADVOCATE,

Petitioner,

v.

FREEHOLD COGENERATION ASSOCIATES, L.P.,

Respondent.

ON PETITIONS FOR A WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION TO PETITIONS FOR A WRIT OF CERTIORARI

ROBERT F. SHAPIRO
Counsel of Record
LYNN N. HARGIS
MARTIN W. GITLIN
Chadbourne & Parke
1101 Vermont Avenue, N.W.
Washington, D.C. 20005
(202) 289-3000
Attorneys for Respondent Freehold Cogeneration Associates, L.P.

July 5, 1995

QUESTION PRESENTED

Whether Section 210(e) of the Public Utility Regulatory Policies Act of 1978 ("PURPA") and the Federal Energy Regulatory Commission's implementing regulations, which exempt qualifying cogeneration facilities from state rate regulation, preempt the New Jersey regulatory agency from modifying the rates of a qualifying cogeneration facility in a long-term contract where those rates were "locked-in" and approved by the agency under another provision of PURPA in orders that were not challenged and that have become final and nonappealable.

RULE 29.1 LIST

Respondent Freehold Cogeneration Associates, L.P. ("Freehold") is a limited partnership. Constellation Energy, Inc., through wholly-owned subsidiaries, owns a 1 percent general partnership interest and a 49 percent limited partnership interest in Freehold. Constellation Energy, Inc. is a wholly-owned subsidiary of Constellation Holdings, Inc., which, in turn, is a wholly-owned subsidiary of Baltimore Gas & Electric Company, a publicly traded company. The other general partner in Freehold is APS Freehold, Inc., with a 1 percent general partnership interest. APS Freehold, Inc. is a privately held corporation. The remaining limited partnership interest in Freehold (49 percent) is held by APS Associates, L.P. APS Associates, L.P. comprises Advanced Power Systems, Inc., a privately held corporation owning a 98 percent general partnership interest, and Interstate Business Corporation and Wilson Securities Corporation, each a privately held corporation owning a 1 percent limited partnership interest.

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STATEMENT OF THE CASE

I. NATURE OF THE CASE

Respondent Freehold Cogeneration Associates, L.P. ("Freehold") is a "qualifying cogeneration facility" ("qualifying facility" or "QF") under the Public Utility

Regulatory Policies Act of 1978, Pub.L.No. 95-617, 92 Stat. 3117 (1978) ("PURPA"). Pursuant to one section of PURPA, the Federal Energy Regulatory Commission ("FERC") issued rules, to be implemented by the states, that established, *inter alia*, the rates that utilities must pay for the purchase of electricity from qualifying facilities. Pursuant to another section of PURPA, the FERC issued rules that are self-effectuating, *i.e.*, not to be implemented by the states, exempting QFs from all state laws and regulations respecting rates and financial and organizational regulation of utilities.

In 1992, the New Jersey Board of Regulatory Commissioners ("BRC") implemented the FERC rules by approving the rates contained in a long-term power purchase agreement ("PPA") between Freehold and Jersey Central Power & Light Company ("Jersey Central") for the life of the PPA. The BRC's order was never challenged and is final and nonappealable. Freehold contended, and the United States Court of Appeals for the Third Circuit held in the *"Freehold"* decision below,[1] that, once the rates in the PPA were determined by the BRC to be just and reasonable and prudently incurred for the life of the PPA in a final and nonappealable order, the BRC's implementation under PURPA ceased. Consequently, its requirement in 1994 that Freehold renegotiate those rates or submit to a hearing that would lead to a modification of the rates or withdrawal of the BRC's prior approval is preempted by PURPA and the FERC's implementing regulations. Those regulations specifically allow qualifying facilities to lock-in the rates for

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[1] *Freehold Cogeneration Associates, L.P. v. Board of Regulatory Commissioners of the State of New Jersey,* 44 F.3d 1178 (3rd. Cir. 1995). (Pet. App. A-1 - A-29).

the life of the contract and exempt qualifying facilities from rate regulation by the states.

The Third Circuit's decision below is consistent with PURPA and the FERC's implementing regulations and with the two high appellate court decisions that have addressed the issue of a state's right to revisit the rates in a QF contract once they have been established. There is no compelling reason to hear this case.

II. THE STATUTORY AND REGULATORY SCHEME

A. Federal Power Act

In 1935, the Congress enacted Part II of the Federal Power Act ("FPA"), 16 U.S.C. §§ 824-824k (1988), which delegated to the Federal Power Commission (now the FERC) the exclusive authority to regulate the rates for the transmission and sale at wholesale of electric energy in interstate commerce. *United States v. Pub. Utils. Comm'n of Cal.*, 345 U.S. 295 (1953). The legislation was a "direct result" of this Court's holding in *Pub. Utils. Comm'n v. Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927) that the states lacked authority to regulate the rates for interstate sales of electricity for resale. *United States v. Pub. Utils. Comm'n of Cal., supra*, 345 U.S. at 311. *See Jersey Central Power & Light Co. v. Fed. Power Comm'n*, 319 U.S. 61, 67-68 (1943); *Fed. Power Comm'n v. Southern California Edison Co.*, 376 U.S. 205, 215-216 (1964).

B. PURPA

In 1978 Congress passed PURPA as part of comprehensive national energy legislation to address the nation's energy crisis. *See Fed. Energy Reg. Comm'n v. Miss.*, 456 U.S. 742, 745-6 (1982). To make the nation more energy independent, the Congress determined that certain types of electricity production facilities were to be encouraged because they provide important benefits to society. *Id.* at 745-6, 750. Those facilities include small power production facilities that use renewable energy sources such as solar, wind, biomass and water, and cogeneration facilities that use fuel more efficiently by sequentially producing from that fuel both electricity and useful thermal energy (usually in the form of steam) for manufacturing or heating purposes. *Id.* at 750, n.11. PURPA represents a marked, albeit limited, departure from the traditional regulatory scheme, under which the FERC exercises exclusive jurisdiction over wholesale rates in interstate commerce. Under PURPA, the contract rates for a utility's wholesale purchases from QFs are determined according to regulations promulgated by the FERC, but implemented by state utility commissions.

1. Section 210 of PURPA

The QF provisions of PURPA reflect Congress' determination that there were two chief impediments to encouraging such non-utility energy producers: (1) utilities were reluctant to buy power from them; and (2) such power producers themselves were reluctant to shoulder the burdens of traditional utility regulation. *Id.* at 750-51. To overcome these impediments, Congress, in enacting Section 210 of PURPA ("Section 210"), provided a framework for federal and state implementation of utility purchase obligations and ratemaking principles, exemption from federal and state utility regulation, and certain judicial review mechanisms.

Section 210(a), 16 U.S.C. § 824a-3(a) (1988), directed the FERC to prescribe "such rules as it determines necessary to encourage cogeneration," which would require electric utilities to offer to purchase electric energy from, and sell back-up and other necessary energy to, such qualifying facilities.

Section 210(b), 16 U.S.C. § 824a-3(b), provides that the regulations promulgated by the FERC under Section 210(a) shall ensure that the rates for the purchase of power from a QF shall be "just and reasonable" to the electric consumers of the purchasing electric utility, and shall not exceed the incremental cost to the electric utility of alternative electric energy. This incremental cost of alternative electric energy is commonly referred to as the electric utility's "avoided cost."[2]

However, the conference committee report accompanying PURPA made it clear that in referring to the term "just and reasonable":

> It is not the intention of the conferees that cogenerators and small power producers become subject, by virtue of this language, and the rules promulgated under this section, to the type of examination that is traditionally given to electric utility rate applications to determine what is the just and reasonable rate that they should receive for their

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2 Section 210(d) defines the term "incremental cost of alternative electric energy" used in Section 210(b) for purchases from QFs as: "the cost to the electric utility of the electric energy which, but for the purchase from such cogenerator or small power producer, such utility would generate or purchase from another source."

> electric power. The conferees recognize that cogenerators and small power producers are different from electric utilities, not being guaranteed a rate of return on their activities generally or on the activities vis-à-vis the sale of power to the utility and whose risk in proceeding forward in the cogeneration or small power production enterprise is not guaranteed to be recoverable.

H.R. Conf. Rep. No. 1750, 95th Cong. 2d. Sess. (Oct. 10, 1978) *reprinted in* 1978 U.S.C.C.A.N. (92 Stat.) 7831-32. The conference report continued:

> The establishment of utility type regulation over them would act as a significant disincentive to firms interested in cogeneration and small power production.

Id. at 7832.

In keeping with this clear Congressional purpose, Section 210(e), 16 U.S.C. § 824a-3(e), authorizes the FERC to issue rules to exempt QFs from "state laws and regulations respecting the rates, or respecting the financial and organizational regulation of electric utilities" and from federal utility regulation.

Section 210(f), 16 U.S.C. § 824a-3(f), provides for state implementation of the FERC's rules promulgated under Section 210(a).

Section 210(g), 16 U.S.C. § 824a-3(g), specifies that judicial review respecting any proceeding conducted by a state regulatory authority for purposes of implementing any requirement under Section 210(a) can be had pursuant to the same conditions as specified under Section 123 of PURPA, 16 U.S.C. § 2633(a) (*i.e.*, in state court). Section

210(h)(2)(B), 16 U.S.C. § 824a-3(h)(2)(B), permits qualifying facilities to petition the FERC to enforce the state's implementation of the FERC's rules as mandated by Section 210(f) and, if the FERC does not initiate an enforcement action within 60 days, authorizes the QF to bring an enforcement action in the appropriate United States district court. Sections 210(g) and (h), therefore, by their terms specifically apply to review of the state implementation of the FERC's rules promulgated under Sections 210(a) and (f). Neither Section 210(g) nor (h) requires that proceedings respecting rules promulgated by FERC pursuant to Section 210(e), authorizing FERC to exempt QFs from certain regulation, be initiated in any particular forum.

2. The FERC's Rules Under Section 210(a) (Purchase at Avoided Cost)

In issuing rules under Section 210(a), the FERC determined that the rate at which a utility would be required to purchase power from QFs would be equal to the utility's full avoided cost. 18 C.F.R. §§ 292.101(b)(6), 292.304(b)(2) (1994). Upon a challenge to these regulations, this Court held that a rate for QF power equal to the utility's full avoided cost is just and reasonable to the electric consumers of the electric utility and fully in accordance with Sections 210(a) and (b) of PURPA. *Am. Paper Inst., Inc. v. Am. Elec. Power Serv. Corp.*, 461 U.S. 402 (1983).

The FERC's rules implementing Section 210(a) provide that if a QF sells electric energy or capacity pursuant to a legally enforceable obligation over a specified term, the rates for such purchases shall, at the option of the QF, be based on the utility's avoided costs as calculated either (1) at the time of the delivery of the power, or (2) at the time the obligation is incurred. 18 C.F.R. § 292.304(d)(2) (1994). The FERC's regulations further provide that, where

the rates are based on avoided costs calculated at the time the obligation is incurred (the so-called "lock-in" right), "the rates for such purchases do not violate [FERC's regulations or PURPA] if the rates for such purchases differ from avoided costs at the time of delivery." 18 C.F.R. § 292.304(b)(5) (1994).

Thus, the FERC explicitly recognized that a utility's avoided costs might change over time, but that any such change subsequent to the QF's incurring a legally enforceable obligation[3] to provide power to the utility would not cause that obligation to violate PURPA or the rules promulgated thereunder. *See Small Power Prod. and Cogeneration Facilities; Regulations Implementing Section 210 of PURPA*, Order No. 69, 45 Fed Reg. 12,214, 12,224 (Feb. 25, 1980) ("The import of this section is to ensure that a qualifying facility which has obtained the certainty of an arrangement is not deprived of the benefits of its commitment as a result of changed circumstances."), *aff'd in part and vacated in part, Am. Elec. Power Serv. Corp. v. Fed. Energy Reg. Comm'n*, 675 F.2d 1226 (D.C. Cir. 1982), *rev'd in part, Am. Paper Inst. v. Am. Elec. Power Serv. Corp.*, 461 U.S. 402 (1983); *West Penn Power Co.*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,153 (1995); *New York State Elec. & Gas Co.*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,027 (1995).

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3 The FERC used the term "legally enforceable obligation" in its rules to encompass obligations that did not rise to the level of an executed contract. As the Commission explained in its preamble to the regulations: "Use of the term 'legally enforceable obligation' is intended to prevent a utility from circumventing the requirement that provides capacity credit for an eligible facility merely by refusing to enter into a contract with the qualifying facility." 45 Fed. Reg. at 12,224 (February 25, 1980).

3. Section 210(e) and the FERC's Rules Thereunder (Exemption from Utility Regulation)

To remove the second impediment to QF development identified by Congress, the burdens of traditional utility regulation, Section 210(e) authorizes the FERC to promulgate rules to exempt QFs from both federal and state utility regulation if it determines such exemption is necessary to encourage cogeneration and small power production. Pursuant to Section 210(e), the FERC issued rules exempting QFs from most federal utility regulation and from all state laws and regulations regarding rates and the financial and organizational regulation of utilities. 18 C.F.R. §§ 292.601 and 292.602 (1994).

C. Implementation of the FERC's Rules

The provisions for implementing the FERC's rules are unusual. Section 210(f) provides that each state regulatory authority must implement the FERC's rules under Section 210(a) for each electric utility for which it has ratemaking authority. Thus, despite the fact that wholesale electricity rates are the exclusive province of the FERC, *see United States v. Pub. Utils. Comm'n of Cal.*, *supra*, PURPA carved out a limited exception to this rule by requiring the states to implement one portion of the federal regulations under PURPA. *See Fed. Energy Reg. Comm'n v. Miss.*, 456 U.S. at 759-761.

III. FACTUAL BACKGROUND

Freehold is constructing a qualifying cogeneration facility in Freehold, New Jersey. In 1989, the BRC issued an order (reproduced at App. A to this Brief) exempting, or "grandfathering," the Freehold project from the BRC's 1989 competitive bidding procedure for the acquisition of new

capacity for New Jersey utilities. As the 1989 order indicated, the new procedure expressly provided that the BRC would determine on a case-by-case basis whether to exempt a particular project, and Freehold was one of a number of projects that it exempted. Jersey Central opposed Freehold's request to be exempted, but did not appeal the BRC's order approving that request. Nor did the New Jersey Division of The Ratepayer Advocate ("DRA") or anyone else appeal. That order is final and nonappealable.

The BRC's 1989 order directed Freehold and Jersey Central to negotiate a contract with pricing tied to the benchmark price contained in Jersey Central's 1989 competitive bidding solicitation. After more than 2 years of negotiations, the parties signed the PPA on March 26, 1992.

On March 31, 1992, Jersey Central submitted the PPA to the BRC for approval (letter accompanying submittal is reproduced at App. B). In doing so, Jersey Central expressly argued that the contract rates should be protected for the life of the contract:

> Principles of equity dictate that the Board provide both the purchasing utility and the cogenerator with sufficient assurances that the avoided costs contract rate, once approved by the Board, will not be subject to further scrutiny. In this regard, FERC has indicated that neither the purchasing utility nor the QF are to be deprived of the mutual benefits of entering into a long-term contract based on Board approved avoided cost rates. In order to preserve the benefit of the bargain between the utility and the QF, flow-through of the purchased power costs incurred under this or similar agreements must be assured.
>
> In the instant case, both JCP&L and Freehold need to have the certainty that neither this nor future

> Boards will impair the utility's right to flow-through to and/or fully and timely recover from its ratepayers the contracted for, and Board-approved, purchase price over the full term of the Agreement or exercise jurisdiction over this or similar agreements.

App. B-3.

The BRC issued an order approving the PPA on July 8, 1992. (Reproduced at App. C). In that order, the BRC stated that "the price is equal to 100% of the applicable avoided cost" (App. C-5), and found that:

> the rates specified and the costs resulting therefrom [are] reasonable and reasonably and prudently incurred by JCP&L throughout the full term of the Agreement. Therefore the Board and its successors will allow JCP&L to flow-through and/or fully and timely recover the rates specified in the Agreement....

Id. (Emphasis added). Neither Jersey Central nor any other party, including the DRA, opposed approval of the PPA. Neither Jersey Central nor any other party sought appellate review of the Board's order approving the PPA. That order is final and nonappealable.

The BRC issued an order, dated April 12, 1993 (the "Towner Order"), directing electric utilities in New Jersey to assess their existing contracts with qualifying facilities under PURPA and to bring to its attention any contracts that the utilities believed no longer were economic. Jersey Central informed the BRC that the Freehold PPA might be a candidate for buyout or modification. Freehold then met with the BRC's staff and voluntarily agreed to certain price concessions in exchange for certain nonprice modifications to the PPA.

On January 4, 1994, the BRC issued an order pursuant to purported state authority rejecting the voluntary agreement between Freehold and the BRC's staff and directing Freehold and Jersey Central to renegotiate the rates in the PPA or to negotiate a buyout of the PPA. If no agreement was reached within thirty (30) days, the BRC would commence an evidentiary hearing to consider revoking its prior approval of the PPA. (Order reproduced at App. D). When no agreement was reached, the BRC issued an order commencing evidentiary hearings. (Order reproduced at App. E). The hearings continued from March, 1994 through the beginning of January, 1995, when they were halted as a result of the Third Circuit's decision below.

The Third Circuit's decision was a direct result of a Complaint filed by Freehold against the BRC and Jersey Central in the United States District Court for the District of New Jersey. The Complaint alleged that the BRC was preempted under PURPA and the FERC's implementing regulations from revisiting the order approving the PPA and the rates contained therein. The district court dismissed the Complaint on jurisdictional grounds.

IV. THE DECISION BELOW

In a unanimous decision, the Third Circuit reversed the district court, finding that the court not only had jurisdiction, but also that federal law preempted the BRC from revisiting its prior approval of the PPA and its rates:

> Based on the overall scheme of PURPA and its stated goal, and especially section 210(e) and the implementing rules promulgated by the FERC, we hold that Congress intended to exempt qualified cogenerators from state and federal utility rate regulations.

Freehold, 44 F.3d at 1192. (Pet. App. A-24). The court found that once the BRC had completed its implementation of Section 210(a) by its 1992 order approving the PPA, its present attempt to modify the PPA or revoke its prior order constituted "exactly the type of regulation from which Freehold is immune under section 210(e)." *Id.*

The court went on to explain that its decision was consistent with two recent high appellate court decisions: *Indep. Energy Producers Ass'n v. Cal. Pub. Utils. Comm'n*, 36 F.3d 848 (9th Cir. 1984) and *Smith Cogeneration Management, Inc. v. Corp. Comm'n*, 863 P.2d 1227 (Okla. 1993). The court also reviewed the so-called "regulatory-out" clause in the PPA, which it found to be "unambiguous," and determined that:

> this clause does not purport to confer on the BRC any jurisdiction it would not otherwise have. In particular, it reflects no intent on the part of Freehold to surrender any of the protection from state rate regulation conferred upon it by section 210(e).

Freehold, 44 F.3d at 1194 (Pet. App. A-28).

Jersey Central, the BRC, and the DRA filed a request for rehearing of the panel and of the Third Circuit *en banc*, which was denied on March 7, 1995. Two weeks after rehearing was denied, Jersey Central filed a petition with the FERC, asking the FERC to void the PPA notwithstanding the Third Circuit's decision. That petition is still pending. Jersey Central and the DRA filed their petitions for a writ of certiorari with this Court on June 5, 1995. The BRC did not file a petition.

REASONS FOR DENYING THE WRIT

I. NEITHER THE NEW JERSEY BOARD OF REGULATORY COMMISSIONERS, THE APPELLEE BELOW, NOR THE FEDERAL ENERGY REGULATORY COMMISSION, THE AGENCY WHOSE RULES ARE BEING APPLIED, ARE CHALLENGING THE THIRD CIRCUIT'S HOLDING

As discussed *supra* in the Statement of the Case, the issue in this case is whether the actions of the BRC are preempted by PURPA and the implementing regulations promulgated by the FERC. Tellingly, the New Jersey state agency whose actions are at issue here appears to have accepted the decision of the Third Circuit. Conspicuously absent from these proceedings is a petition by the BRC for a writ of *certiorari*, an absence that suggests that the BRC can live with the *Freehold* decision.[4]

Similarly, the federal government is not troubled by the merits of this case. In response to the Third Circuit's request below to brief the jurisdictional issues and "any of the other issues raised by this appeal that it desires to" (*See* App. F to this Brief for the text of the court's order), the FERC filed a brief *amicus curiae* addressing the jurisdictional issues in the case but expressly declined the court's invitation to address the merits. On all the jurisdictional issues, the FERC sided with Freehold, advocating the same position that the court ultimately adopted. (The FERC's *amicus* brief is

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4 On June 26, 1995, the BRC filed Notices of Appearance with this Court in these proceedings in which it specifically stated that it would not be filing a brief in this matter.

reproduced at App. G). More recently, the FERC has cited the Third Circuit's decision with approval. *See, e.g., Conn. Light & Power Co.*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,035 at 61,152 (1995) (the Third Circuit's *Freehold* decision "supports our conclusion").

Both the BRC's and the FERC's acceptance of the Third Circuit's decision fully justifies this Court's denial of the writ.

II. THE THIRD CIRCUIT'S HOLDING IS FULLY CONSISTENT WITH THE OTHER HIGH APPELLATE COURT DECISIONS THAT HAVE ADDRESSED ATTEMPTS TO REVISIT AN APPROVED QF CONTRACT

The Court of Appeals' decision, far from conflicting with the decisions of other appellate courts and the FERC, as suggested by Jersey Central (Pet. at 13), is fully consistent with the two other high appellate court decisions that have addressed whether a state may reconsider the rates paid to a QF under a power purchase contract.

In *Indep. Energy Producers Ass'n, Inc. v. Cal. Pub. Utils. Comm'n*, 36 F.3d 848 (9th Cir. 1994), the United States Court of Appeals for the Ninth Circuit struck down a program under which the California Public Utilities Commission ("CPUC") permitted the utilities to reduce the rates paid to QFs under long-term contracts if the utilities determined that the QFs did not meet certain criteria established by the FERC's regulations implementing PURPA. In reviewing the program, the court observed that:

> The underlying motivation behind the CPUC program is to lower the rates set in [the utilities'] standard offer contracts because they are higher than the Utilities' current avoided costs. [T]his differential

> exists because the standard offer contracts lock the Utilities into paying rates that were calculated on incorrect assumptions about the future cost of fossil fuels.

Id., 36 F.3d at 858. As to that "underlying motivation," however, the court found that, notwithstanding the "incorrect assumptions" attendant to the original approval of the contract, PURPA and the FERC's implementing regulations precluded the CPUC and the utilities from unilaterally changing the rates once they had been locked-in by contract:

> The fact that the prices for fuel, and therefore the Utilities' avoided costs, are lower than estimated, does not give the state and the Utilities the right unilaterally to modify the terms of the standard offer contract. * * * [In promulgating its regulations implementing PURPA, t]he Commission recognized that, at times, the avoided cost rate provided in the contract might be greater or less than the utility's current avoided costs but that certainty as to rate was important....

Id., 36 F.3d at 858 (Citing to the FERC's preamble to its PURPA rules). This is consistent with the holding of the Third Circuit below. *See Freehold*, 44 F.3d at 1194 (Pet App. A-28 - A-29). Once Freehold and Jersey Central established the rates in the PPA and the BRC's order approving those rates became final and nonappealable, the BRC and Jersey Central were precluded from changing those rates unilaterally.

The Third Circuit's holding also is consistent with a recent decision of Oklahoma's highest court. *Smith Cogeneration Management, Inc. v. Corp. Comm'n*, 863 P.2d 1227 (Okla. 1993). There the court held that PURPA deprives the state regulatory commission of authority to revisit the avoided cost rates in a QF contract once they have

been established. *Id.*, 863 P.2d at 1241. The court invalidated a state regulatory commission rule that required utilities to include in their contracts with QFs a clause allowing the commission to modify the terms and conditions of the contract during the term of the contract. It found that "[r]econsideration of long-term contracts with established estimated avoided costs imposes utility-type regulation of QFs. PURPA and FERC regulations seek to prevent reconsideration of such contracts." *Id.*, 863 P.2d at 1240. The court concluded that the "Corporation Commission rules, to the extent which they require qualifying facilities to include a notice provision allowing reconsideration of avoided costs after the contract is agreed upon, are preempted by federal law." *Id.*, 863 P.2d at 1242. The analysis and conclusion of the Oklahoma court apply equally to the BRC's attempt to revisit Freehold's rates nearly two years after approving them in a final and nonappealable order, as the Third Circuit correctly held. *See Freehold*, 44 F.3d at 1193 (Pet. App. A-25 - A-26).

III. THE THIRD CIRCUIT'S DECISION IS CONSISTENT WITH RECENT DECISIONS BY THE FERC INTERPRETING PURPA AND ITS REGULATIONS

The Third Circuit's decision also is fully consistent with the interpretation of PURPA and its regulations advanced by the FERC, the agency charged with implementing and administering the statute. On several recent occasions, the FERC has considered and rejected requests by utilities to declare the rates contained in their power purchase contracts with QFs to be invalid. *See, e.g., West Penn Power Co.*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,153 (1995); *New York State Elec. & Gas Corp.*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,027 (1995) (*"NYSEG"*); *Metro. Edison Co./Penn. Elec. Co.*, Docket

No. EL95-41-000 (approved by vote of the FERC on June 28, 1995).[5]

In *NYSEG*, for example, the utility sought an order from the FERC to relieve it of its obligation to purchase energy from two QFs at rates that had been established in separate power purchase contracts that had been approved by the state commission in final and nonappealable orders. The utility's purported justification for its request was that circumstances had changed since the contracts were executed, resulting in a situation in which the rates contained in the contracts exceeded its then-current avoided cost. The FERC denied the utility's petition, holding that, under its regulations, the contract rates were established (*i.e.*, "locked-in") at the time of contracting.

Specifically, the FERC noted that its regulations provide that the rates under a power purchase contract do not violate PURPA if they differ from avoided costs at the time the electricity is delivered. 71 Fed. Energy Reg. Comm'n Rep. at 61,116, citing 18 C.F.R. § 292.304(b)(5) (1994). Those regulations were promulgated in the belief that "in the long run, 'overestimations' and 'underestimations' will balance out" and that the lock-in of the rates would "ensure that a [QF] which has obtained the certainty of an arrangement is not deprived of the benefits of its commitment as a result of changed circumstances." *Id.*, citing *Small Power Prod. and Cogeneration Facilities*, 45 Fed. Reg. at 12224 (Feb. 5, 1980). (See App. H to this Brief for text of *NYSEG* order.)

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5 Metropolitan Edison Company and Pennsylvania Electric Company are utility affiliates of Jersey Central and are owned by a common parent, General Public Utilities Corp.

This is the same holding as that adopted by the Third Circuit below: once the purchase rates for electricity sold by a QF to a utility have been locked-in and approved, those rates may not be changed unilaterally by the utility or the state commission as a result of changed circumstances. *See also West Penn*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) at 61,495-96 (rejecting utility's assertion that changed circumstances -- *i.e.*, decreases in its projections of avoided cost from those contained in power purchase contract with the QF -- justified reduction of the rates it paid under that contract, which had been approved by the state commission in a final and nonappealable order). (*See* App. I to this Brief for the text of the *West Penn* order.)

IV. JERSEY CENTRAL'S ALLEGATIONS OF A LARGE DISPARITY BETWEEN AVOIDED COSTS AND THE RATES THAT IT WILL PAY UNDER THE PPA ARE WHOLLY UNSUBSTANTIATED AND ARE IRRELEVANT IN ANY EVENT

Jersey Central argues that this Court should grant the writ because of the "disbenefits" that the PPA allegedly will cause to Jersey Central's ratepayers (Pet. at 8, 13-14). Jersey Central completely fails, however, to offer any support for its claims.

Jersey Central argues that at the time the BRC approved the PPA in 1992, the rates specified therein exceeded its avoided cost. When Jersey Central submitted the PPA for BRC approval, however, it never suggested that the rates exceeded its avoided cost. Indeed, it argued that the rates contained in the PPA should be protected for the life of the PPA. See Factual Background, *supra*, at 9-12. When the BRC approved the PPA, it specifically held that the rates were "equal to 100% of the applicable avoided cost." (App.

C-5). No party challenged that determination. Even when the BRC sought to revisit the rates under the PPA, it did so on the basis that estimates of avoided costs had declined since the PPA was approved (*see* App. D-4, 11, 12, E-2), rather than on any alleged mismatch at the time of contracting. Thus, Jersey Central's claim amounts to little more than a *post hoc* rationalization that rings hollow here.

PURPA was enacted because utilities refused to deal with cogenerators and small power producers. *Fed. Energy Reg. Comm'n v. Miss.*, 456 U.S. at 750-51. Absent PURPA, there would have been no cogeneration contracts. The utilities would have continued their construction on the traditional "cost plus" basis and there would have been no competition for generating capacity. PURPA helped to establish the competitive market for generation by requiring utilities to stop their anticompetitive actions and start acting in the best interests of the nation. In the absence of cogeneration, traditional utility construction would have led to far higher rates for electric consumers.[6]

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6 Jersey Central's claim (Pet. at 14) that the PPA will result in excessive costs to ratepayers compared to current market alternatives is wildly inaccurate. Under the utility's market test, nearly all of Jersey Central's existing generating capacity would be found to be excessively expensive as well. Moreover, Jersey Central neglects to point out that, absent PURPA, utilities would have continued to build plants like the Three Mile Island II nuclear unit, partly owned by Jersey Central, which has cost ratepayers hundreds of millions of dollars without providing any electricity. Under the PPA, in contrast, Freehold only gets paid if it performs properly. As for the *Wall Street Journal* article cited by Jersey Central (Pet. at 14), the reporter was demonstrably biased, focusing primarily on exotic technologies that have experienced problems, not on the hundreds of conventional cogeneration plants, like the Freehold project, that have provided and will provide reliable, cost-effective power.

Further, to the extent that there have been decreases in avoided costs since the rates under the PPA were locked-in, as Jersey Central has suggested (Pet. at 8), the FERC, in its implementing rules, specifically contemplated that such changes might occur, but found that the potential for such changes was outweighed by the importance of providing the certainty required for financing of QF projects. *See Small Power Prod. and Cogeneration Facilities*, 45 Fed. Reg. at 12,224; *NYSEG, supra.*

In any event, the relationship between Jersey Central's current avoided cost and the rates under the PPA is irrelevant for purposes of this case. As is discussed in greater detail *infra*, once the BRC approved the rates in a final and nonappealable order, its implementation of the FERC's avoided cost regulations was at an end. Section 210(e) of PURPA and the FERC's regulations promulgated thereunder at 18 C.F.R. § 292.602(c) (1994) specifically exempt Freehold from state rate regulation. Consequently, the BRC lacks authority to modify the rates in the approved PPA, as the Third Circuit correctly held.

V. FERC'S IMPLEMENTING REGULATIONS ARE NO LONGER SUBJECT TO CHALLENGE

The provisions of Section 210 of PURPA are not self-implementing. Rather, PURPA Section 210 is given effect through the issuance of rules by the FERC. These rules have the "force of law." *See United States v. Nixon*, 418 U.S. 683, 694-96 (1974). Thus, Jersey Central's reference to the statutory requirements of PURPA instead of the FERC's implementing regulations (Pet. at 22) is unavailing.

The FERC issued its regulations respecting the rates for the purchase of power from QFs, including the right of a QF to the "lock-in" estimates of avoided cost, in 1980. They were affirmed by this Court in 1983. *Am. Paper Inst., supra.*

For 15 years, these rules have been consistently applied and relied upon by an entire industry. It is far too late to challenge them now. Indeed, the United States Court of Appeals for the District of Columbia Circuit, on review of the FERC's rules implementing PURPA, expressly observed in 1982 that the time to challenge them was when they were promulgated, not years later:

> Thus, if petitioners fail to pursue their remedies now, they do so at their peril of losing the right ever to challenge the validity of the Commission's regulations.

Am. Elec. Power Serv. Corp. v. Fed. Energy Reg. Comm'n, 675 F.2d 1226, 1232 (D.C. Cir. 1982), *rev'd on other grounds sub nom., Am. Paper Inst. v. Am. Elec. Power Serv. Corp.*, 461 U.S. 402 (1983). *See also NYSEG*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) at 61,116 (App. H-32), ("It is now far too late in the Commission's implementation of PURPA for NYSEG to argue, for the first time, that these particular regulations have legal and policy flaws requiring that we abrogate contracts entered into under these regulations.") (emphasis in original).

VI. FREEHOLD PRESENTED A VALID CLAIM THAT IT IS EXEMPT FROM RATE REGULATION UNDER SECTION 210(e)

A. As an Action Under Section 210(e) of PURPA, Jurisdiction Over This Matter Properly Resided with the Federal Courts

The Third Circuit correctly held that the district court had jurisdiction over Freehold's claim and that the jurisdictional bar contained in Section 210(g) applies only to those portions of Section 210 that require utilities to purchase energy from and sell energy to qualifying facilities (Section 210(a)), and to the requirement that state authorities implement the federal rules (Section 210(f)).

Freehold did not challenge the BRC's implementation pursuant to Section 210(f) of the FERC's rules under Section 210(a). Rather, Freehold brought this proceeding under Section 210(e) and the FERC's rules implementing that section, 18 C.F.R. § 292.602(c) (1994). Indeed, the BRC admits that the challenged order of the BRC was not issued to implement the FERC's rules, but pursuant to purported state law.[7] See App. D-12, E-6, E-7. In its brief *amicus curiae* to the Third Circuit, the FERC agreed that Freehold presented a valid claim under Section 210(e), and that the federal court had jurisdiction over that claim. *See* App.

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7 The BRC consistently has cited state law as its authority to hold the hearings to revise or revoke the PPA. (*e.g.*, App. D-12, E-6, 7). Further, in arguing in the district court against the assertion of federal jurisdiction over this matter, the BRC consistently invoked its purported powers under state law, 48:2-40, to "revoke or modify an order made by it." There thus can be no legitimate dispute that the BRC proceeded under state law to regulate Freehold's rates.

G-14. *See Shaw v. Delta Airlines*, 463 U.S. 85 (1983) ("It is beyond dispute that federal courts have jurisdiction over suits to enjoin state officials from interfering with federal rights...").

In asserting that Section 210(g) of PURPA deprives the federal courts of jurisdiction, Jersey Central mischaracterizes the holding in *Bristol Energy Corp. v. N.H. Public Utils. Comm'n*, 13 F.3d 471 (1st Cir. 1994). In *Bristol Energy*, the First Circuit, on review, held that the federal courts have jurisdiction over a Section 210(e) claim:

> We have considered -- and we reject -- PUC's argument that 16 U.S.C. § 824a-3(g) divests federal courts of jurisdiction. Section 824a-3(g) places limits on federal jurisdiction in proceedings involving rules implementing 16 U.S.C. §§ 824a-3(a) and -3(f), rules not at issue in this case.... We conclude that federal question jurisdiction exists in this case, ... because plaintiffs allege a preemption claim and seek to enjoin state officials from interfering with a federal right, i.e., the QF exemption.

13 F.3d at 474 (emphasis supplied). The QF exemption is the Section 210(e) exemption.

The jurisdictional issue in the present case is virtually identical to that in the *Bristol Energy* case. On that issue the First Circuit determined that the limitations on federal jurisdiction imposed by Section 210(g) are inapplicable where, as here, plaintiffs "allege a preemption claim and seek to enjoin state officials from interfering with a federal right,

i.e., the QF exemption." *Id.*[8] The Third Circuit reached the same result below. *See also Indep. Energy Producers, supra,* (district court exercised jurisdiction to hear a claim that the state agency action that permitted modification of approved QF contract rates was preempted by PURPA).

B. The BRC Impermissibly Sought to Regulate Freehold's Rates After They Had Been Locked-In and Approved

In its January 5, 1994 order directing Jersey Central and Freehold to negotiate a buy-out or reformation of the PPA (App. D) and in its March 7, 1994 order instituting proceedings to reform the rates under the PPA or revoke its earlier approval of the PPA (App. E), the BRC impermissibly attempted to regulate the rates to be paid by Jersey Central to Freehold under the PPA. Indeed, the BRC's express reason for ordering negotiations and commencing the hearing was because of its view that the rates contained in the PPA exceeded the then-current avoided cost of Jersey Central. *See* App. D-11. Further, both orders were issued under purported authority of the New Jersey regulatory statute. App. D-12, E-7. Nowhere in either order does the Board suggest that its inquiry constitutes continued implementation of PURPA or give any indication that the actions are being pursued under any authority other than state law. Any such state law or regulation that would permit the BRC to modify the rates under the PPA is precisely the type of law or regulation (*i.e.*, those respecting

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8 On the merits, the First Circuit addressed the authority to compel disclosure of data under section 712 of the Energy Policy Act of 1992, a statute that is not implicated in this case.

"rates") from which QFs such as Freehold specifically are exempted pursuant to Section 210(e) of PURPA and the FERC's regulations. Consequently, as the Third Circuit correctly held, the BRC's attempt to modify the rates under the PPA constituted regulation of Freehold's rates, an activity that expressly is preempted by Section 210(e).[9]

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9 Jersey Central, relying on *N.Y. State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 115 S.Ct. 1671, 1682 (1995) and *Cippolone v. Liggett Group, Inc.*, 112 S.Ct. 2608 (1992), argues that the Third Circuit improperly expanded the preemptive effect of PURPA Section 210(e). In fact, neither of these cases supports Jersey Central's claims. Jersey Central cites *Blue Cross*, a case interpreting the preemptive effect of ERISA, for the proposition that the Third Circuit disregarded the presumption that Congress did not intend to supplant state law. In this case, however, it is beyond cavil that Section 210(e), as implemented by the FERC's regulations, expressly exempts QFs from all "State laws and regulations respecting the rates . . . of electric utilities." Consequently, any such presumption is overcome by the plain language of the statute.

Similarly, Jersey Central cites *Cippolone* for the proposition that the Third Circuit has expanded the preemptive scope of Section 210(e) beyond its "express" preemption of "utility-type" regulation to matters beyond the reach of that section. In fact, nowhere in the language of Section 210(e) or the FERC's implementing regulations is there any "express" language discussing "utility-type" regulation. Indeed, despite Jersey Central's attempt to limit "utility-type" regulation to some form of the traditional "cost-of-service" rate regulation to which utilities historically have been subject, that term is nowhere defined in the statute or regulations. Rather, the language of Section 210(e) and 18 C.F.R. § 292.602(c)(1) (1994) plainly exempts QFs from all state laws and regulations "respecting" the "rates" of electric utilities. Thus, to the extent that the BRC attempted, under color of state law, to modify the "rates" contained in the PPA, its action expressly was preempted by PURPA, as the Third Circuit correctly held.

VII. THE "REGULATORY OUT" CLAUSE OF THE PPA DOES NOT CONFER ON THE BRC POWER TO ALTER QF RATES

The so-called "regulatory out" clause contained in Section 20.2(a) of the PPA,[10] by its plain terms, cannot be read as an affirmative grant of authority to the BRC (or, for that matter, to the FERC or any other agency) to regulate Freehold's rates in a manner that otherwise would be impermissible under PURPA and the FERC's regulations, in particular 18 C.F.R. § 292.602(c), exempting qualifying facilities from state laws respecting the rates of electric utilities. The provision does not state that the BRC is granted the right to modify the contract rates or to deny Jersey Central the right to recover from its ratepayers payments made by Jersey Central under the PPA. The provision merely states that, "in the event that the BRC, the FERC or any legislative, judicial, administrative or other governmental agency having jurisdiction over the parties, the Agreement or the transactions contemplated thereby, should disallow in whole or in part or otherwise impair the full and timely recovery by the Company from its customers...", one of several options shall be implemented. The provision does no more than refer to whatever valid jurisdiction exists independently of the contract and address the allocation of risks steming from any exercise of that valid jurisdiction. All parties (plus the Third Circuit) agreed that the clause was unambiguous. The Third Circuit correctly held that "this clause does not purport to confer on the BRC any jurisdiction it would not otherwise have." 44 F.3d at 1194. (Pet. App. A-28). As previously explained (*see* pp. 19-21,

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10 Section 20.2(a) of the PPA is quoted in full in the Third Circuit's decision below. 44 F.3d at 1193, n.12 (Pet. App. A-27, n.12).

supra), the BRC had no preexisting authority to revisit the QF rates it had approved years before.

VIII. THE DIVISION OF THE RATEPAYER ADVOCATE'S CLAIM THAT THE BRC'S APPROVAL OF THE PPA WAS ULTRA VIRES IS BASELESS AND, IN ANY EVENT, UNTIMELY RAISED

The DRA asserts that the PPA is "void ab initio" because the BRC approved rates that were too high and the BRC's action therefore was "ultra vires". (Pet. at 4). This argument is insubstantial. First, the DRA did not raise its ultra vires argument before the district court. Consequently, as the Third Circuit correctly held, 44 F.3d at 1182, n.3 (Pet. App. A-4, n.3), the DRA failed to preserve the issue on appeal and therefore was barred from raising it before the Third Circuit and likewise is barred from raising it here. *See Duignan v. United States*, 274 U.S. 195, 200 (1927) ("It is only in exceptional cases coming here from the federal courts that questions not pressed or passed upon below are reviewed.") Secondly, the DRA's claim is belied by the BRC's express statement in its order approving the PPA that the rates were "equal to 100% of the applicable avoided cost." (App. C-5). The DRA did not challenge Jersey Central's petition for approval of the PPA or the BRC's order approving it, which is final and nonappealable.

CONCLUSION

For the foregoing reasons, the Petitions for a Writ of Certiorari filed by Jersey Central and the DRA should be denied.

Respectfully submitted,

ROBERT F. SHAPIRO
Counsel of Record

LYNN N. HARGIS
MARTIN W. GITLIN
Chadbourne & Parke
1101 Vermont Avenue, N.W.
Washington, D.C. 20005
(202) 289-3000

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